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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Federal State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
	)	
Forward-Looking Mechanism For High Cost Support	)	CC Docket No. 97-160
	)	DA 98-715

COMMENTS OF U S WEST COMMUNICATIONS, INC.
ON PROPOSALS TO REVISE THE METHODOLOGY
FOR DETERMINING UNIVERSAL SERVICE SUPPORT

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SUMMARY

In its Report to Congress, the Commission made the commitment to reconsider its 25/75 decision and of the method for distributing high-cost support prior to implementing the Commission's methodology for determining high-cost support for non-rural LECs. This is critical, because the 25/75 Plan does not ensure that universal service mechanisms will be "specific, predictable, and sufficient" and that rates will be "just, reasonable, and affordable."

Several alternatives to the 25/75 Plan have been proposed. The task is to select an alternative which appropriately targets federal support for the supra high-cost areas in each state where federal support is needed the most. The NARUC Ad Hoc Working Group proposes a High-Cost Funding Plan ("Ad Hoc Plan") which may appear to offer an attractive alternative because of its seeming simplicity. However, upon closer examination, the proposal is complex. Moreover, it rejects the Commission's fundamental premise that support mechanisms should be based upon forward-looking economic costs. The Ad Hoc Plan is replete with state-wide averaging and approximations. And in the final analysis, the Plan proves to be incapable of targeting federal support to the supra high-cost areas who need the most help.

The Telecommunications Industry Analysis Project ("TIAP") analyzes some general recommendations, but not a complete proposal or plan. One option would modify the sharing ratio in the 25/75 Plan to 40/60. However, this does not address the underlying defect in the 25/75 Plan, which is its inability to target the supra

high-cost areas who need the most assistance. Another TIAP recommendation based on so-called density zones is ill-defined and vague.

The South Dakota Public Utilities Commission ("SDPUC") proposes a Variable Benchmark Option where a different benchmark would be established for each state, based upon the state's forward-looking economic cost and the state's ability to fund its share of universal service. The SDPUC also proposes a Variable Support Option where a single nation-wide benchmark would be established, but the amount of federal support for each state would vary depending on the state's ability to fund its share of universal service. While both of these proposals attempt to target the supra high-cost areas which require help under the federal fund, the two options essentially appear to be only at the concept stage and both have many undefined variables which will require extensive fact finding and resolution. We believe that U S WEST's proposed IHCAP offers a simpler alternative for accomplishing these objectives and would be easier to implement by January 1, 1999.

The Colorado Public Utilities Commission Staff proposes a plan called the Variable Share of Federal Support which is similar to the SDPUC's Variable Support Option. The proposal employs some state-wide averaging which detracts from its ability to target specific supra high-cost areas in a state.

U S WEST proposes the Interstate High Cost Affordability Plan ("IHCAP") as an alternative to the 25/75 Plan. The IHCAP is uniquely suited to targeting federal support to the supra high-cost areas in each state and where support is needed the most. The IHCAP preserves the states' role in funding their fair share of universal service support. Finally, the IHCAP is simple and can be implemented for non-rural LECs in all states by January 1, 1999. The IHCAP offers a reasoned and reasonable alternative for the distribution of high-cost support.

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**COMMENTS OF U S WEST COMMUNICATIONS, INC.
ON PROPOSALS TO REVISE THE METHODOLOGY
FOR DETERMINING UNIVERSAL SERVICE SUPPORT**

U S WEST Communications, Inc. ("U S WEST") hereby submits comments in response to the Federal Communications Commission's ("Commission") Notice requesting comments about proposals which have been submitted to modify the Commission's approach to determining support for non-rural carriers providing service to customers located in high-cost, rural, and insular areas.[1]

I. INTRODUCTION

Congress directed the Commission to ensure that universal service mechanisms are "specific, predictable, and sufficient"[2] and that rates be "just, reasonable, and affordable"[3] for the "preservation and advancement of universal

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[1] Public Notice, Common Carrier Bureau Seeks Comment on Proposals to Revise the Methodology for Determining Universal Service Support, DA 98-715, rel. Apr. 15, 1998.

[2] 47 U.S.C. § 254(b)(5).

[3] 47 U.S.C. § 254(b)(1).

service."[4] The Commission has "the ultimate responsibility to implement the universal service mandate of section 254"[5] However, the "states continue to have jurisdiction over implementing universal service mechanisms for intrastate services supplemental to the federal mechanisms . . . ."[6]

The Commission's 25/75 Plan does not fulfill these requirements. However, the Interstate High Cost Affordability Plan ("IHCAP") proposed by U S WEST will ensure that these Congressional mandates are satisfied. It will also accommodate shared federal and state roles and responsibilities in providing support for universal service.

II. THE "25/75 PLAN" DOES NOT SATISFY THE CONGRESSIONAL MANDATE THAT SUPPORT BE SUFFICIENT OR THE MANDATE THAT RATES FOR LOCAL SERVICE BE AFFORDABLE

When the Commission released the Universal Service Order, it adopted a funding plan for the non-rural local exchange carrier ("LEC") high-cost fund which would provide federal funding for only a small portion of the cost of universal service. The Commission concluded that the federal fund would cover only 25% of the forward-looking cost of universal service, and that the states would be responsible for establishing explicit funding mechanisms for the balance of the costs

[4] 47 U.S.C. § 254(b).

[5] In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Report to Congress, FCC 98-67, rel. Apr. 10, 1998 ("Report to Congress") ¶ 203.

[6] Id. ¶ 205.

of providing universal service.[7] This has been referred to as the "25/75" or "75/25" Plan.

The Commission decided to assess interstate revenues collected from end-user customers, but it declined to assess intrastate revenues for the federal high-cost support mechanism, "because we have every reason to believe that the states will participate in the federal-state universal service partnership so that the high-cost mechanisms will be sufficient to guarantee that rates are just, reasonable, and affordable."[8]

In adopting the 25/75 Plan, the Commission created a dilemma for many states who lack the means and the population base to fund 75% of the costs of providing universal service in high-cost areas in their states. Costs are driven principally by density and distance. Today, the cost of providing affordable service in high-cost rural areas is subsidized by implicit subsidies from lower-cost urban areas, and from overpriced business, discretionary, access, and long distance services. The realities of the new competitive marketplace, as well as the specific directives of the 1996 Act require that these implicit subsidies be removed and replaced by specific, predictable and sufficient explicit support.

This can be done fairly easily and painlessly, for example, in some states such as New York, Maryland, and California who each have high-cost areas within

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[7] In the Matter of Federal-State Joint Board on Universal Service, Report and Order, 12 FCC Rcd. 8776, 8888 ¶ 201 (1997) ("Universal Service Order"), on recon., 12 FCC Rcd. 10095 (1997); appeal pending sub nom. Texas Office of Public Utility Counsel v. FCC, No. 97-60421 (5th Cir.).

[8] Id. at 8924-25 ¶ 268.

their state, but who also have large urban populations over which the cost of supporting higher-cost rural areas can be spread with a relatively modest per-customer assessment.

However, rural and less populous states such as Montana, the Dakotas, Wyoming, Vermont, West Virginia, and Mississippi cannot address high-cost support in the same way that more populous states can. They do not have a sufficiently large number of low-cost densely-populated urban centers to provide the necessary support to the high-cost low-density regions in the state. Although many of these costs are currently in intrastate rates, the majority are in higher rates for business, intraLATA toll and intrastate access charges. When these implicit supports are removed, the local rates or per-customer assessments in some states may be so large as to threaten affordability for some customers. As a result of this demographic imbalance, and faced with the prospect of having to fund 75% of all high-cost areas in their state themselves, states such as these could face the difficult choice of raising rates for local service throughout the state to maintain universal service with the probability that local service will ultimately be unaffordable to some customers, or abandoning the commitment to universal service altogether.[9]

[9] The NARUC Ad Hoc Working Group also recognizes this: "It has long been acknowledged that in some areas of the country it is simply very expensive to provide customers with telephone service. To the extent carriers serving these high cost areas cannot average costs with low cost areas, their customers inevitably face high rates, thereby jeopardizing universal service." NARUC Ad Hoc Working Group, High Cost Support: An Alternative Distribution Proposal, filed Apr. 27, 1998 at 7 ("Ad Hoc Plan").

This is not a choice which the states should be required to make. It would clearly be at odds with the Congressional mandate in Section 254(b)(1) that the Commission shall base policies for the preservation and advancement of universal service on the principle that services should be available at "just, reasonable, and affordable rates."

It is because of this dilemma, which the 25/75 federal support mechanism creates for the states, that the Commission has solicited proposals to revise or supplement the 25/75 Plan.[10]

III. THE IHCAP PROVIDES A MECHANISM TO ENSURE THAT HIGH-COST SUPPORT FOR NON-RURAL LECS WILL BE SUFFICIENT WITHOUT CREATING AN UNTENABLE DILEMMA FOR THE STATES

U S WEST is the sponsor of the IHCAP which offers a simple and reasoned alternative to the dilemma which the Commission's 25/75 Plan has created for predominantly rural and less populous states. Like the 25/75 Plan, the IHCAP leaves the primary role for assuring the continued availability of affordable service with the states. But the IHCAP also provides additional federal assistance just for the very high-cost areas in all states.

A. The IHCAP Is A Hierarchy Of Benchmarks Which Differentiates Between: (1) Those Areas Within A State Which Require No Federal Support, (2) Those High-Cost Areas In A State Which Require Some Federal Support, And (3) Those Supra High-Cost Areas In A State Which Require Substantial Federal Support

The IHCAP builds upon the basic cost and revenue architecture of the 25/75 Plan. The IHCAP specifically permits the Commission to target those supra high-

[10] Notice at 1.

cost areas in states such as Montana, Wyoming, Mississippi, West Virginia, and Vermont where the Commission's initial 25/75 proposal to provide federal funding for only 25% of the costs above a single benchmark was admittedly inadequate. Under IHCAP:

(1) The federal fund would provide no explicit support for loop costs for which the forward-looking costs are $30 or less.

(2) The federal fund would provide explicit support for 25% of forward-looking loop costs between a Primary Benchmark of $30 and a Super Benchmark of $50, and the states would provide support for 75% of the costs between these Benchmarks as they do under the Commission's 25/75 Plan.

(3) For those supra high-cost areas where the per-customer cost of supporting universal service under the Commission's 25/75 Plan could become so high that service could become unaffordable, the IHCAP will provide federal funding for all forward-looking loop costs above the $50 Super Benchmark.

By leaving primary responsibility for most of the costs of universal service with the states, state commissions will be able to devise manageable rate rebalancing and/or explicit funding plans which are right for their local markets and customers. The IHCAP steps in to help those states who have many supra high-cost customers and few low-cost customers, and leaves all states with a manageable problem to solve in removing remaining implicit supports.

The IHCAP results in the minimum interstate fund size to achieve the universal service goals of Congress. It is competitively neutral. Moreover, it is simple and straightforward and it can be implemented by January 1, 1999 for all non-rural LECs.

B. Other Commenters Support The Multi-Benchmark Architecture Of The IHCAP

GTE has voiced support for the concept of multiple benchmarks upon which the IHCAP is based. Like U S WEST, GTE believes that the calculation of the initial level of universal service support should be based on a sliding scale of benchmarks and percentages rather than upon a single benchmark such as that in the 25/75 Plan.[11]

> US West proposed a plan which incorporates a second benchmark. . . . GTE believes that this approach is more promising than the single-benchmark structure; in its earlier comments, GTE has also proposed a two-benchmark plan. The addition to the second benchmark, and the Federal/state split between the two benchmarks, provides the plan with additional degrees of freedom, which in turn will allow the Commission to more accurately target support to meet its policy goals. The second benchmark provides a simple mechanism for supporting high-cost states or areas where rate rebalancing would yield competitively unsustainable, unaffordable rates that threaten universal service.[12]

GTE also suggests some variations to the IHCAP approach for consideration which U S WEST could also support:

(1) 2 Benchmark Plan (Benchmarks of $30 & $50 or $25 & $40):

(a) The federal fund would provide no support for loop costs which are less than the Primary Benchmark of $25 or $30;

(b) The federal fund would provide support for 50% of loop costs between the Primary Benchmark of $25 or $30 and the Super Benchmark of $40 or $50, and the states would provide support

[11] Proposal of GTE, filed Apr. 27, 1998 at 21.

for 50% of the costs between these Benchmarks; and

(c) The federal fund would provide support for 100% of the costs above the Super Benchmark of $40 or $50.

(2) 3 Benchmark Plan ($20, $25, $40)

(a) The federal fund would provide no support for loop costs which are less than the Benchmark of $20;

(b) The federal fund would provide support for 25% of loop costs between the Benchmarks of $20 and $25, and the states would provide support for 75% of the costs between these Benchmarks;

(c) The federal fund would provide support for 50% of the loop costs between the Benchmarks of $25 and $40, and the states would provide support for 50% of the costs between these Benchmarks; and

(d) The federal fund would provide support for 100% of the costs above the Super Benchmark of $40.

These variations on the IHCAP permit even more refined sharing arrangements between the federal fund and the states if the Commission concludes that these additional degrees of granularity would be helpful to carriers and state commissions. However, U S WEST has some concern that introducing additional benchmarks may add levels of complexity which are not required, which may slow implementation, and which may add to the carriers' and the Commission's

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[12] Id. at 21-22 (footnote omitted).

administrative costs of implementing the support mechanisms.

The architectural structure of the IHCAP is sound. Assuming the adoption of a reasonable forward-looking proxy model, U S WEST believes that the 2-Benchmark approach with a Primary Benchmark of $30 and a Super Benchmark of $50 provides the necessary degree of flexibility to be able to provide federal support for the supra high-cost areas. This approach is manageable for non-rural LECs and for the states.

IV. THE NARUC AD HOC PLAN FAILS TO TARGET FEDERAL SUPPORT FOR THOSE STATES WHO NEED IT MOST

The NARUC Ad Hoc Working Group proposes a High-Cost Funding Plan as another alternative.

A. Similarities And Differences Between The Ad Hoc Plan, The 25/75 Plan And The IHCAP

Like the Commission's 25/75 Plan and the IHCAP, the Ad Hoc Plan is a federal support mechanism and it would be funded by a charge on the interstate revenues of interstate carriers. However, unlike the 25/75 Plan and the IHCAP, state support for universal support is not a required element of the Ad Hoc Plan.

Unlike the Commission's 25/75 Plan and the IHCAP which are designed as federal support mechanisms exclusively for non-rural LECs serving high-cost areas,[13] the Ad Hoc Plan would apply to both rural and non-rural LECs. Moreover, unlike the Commission's 25/75 Plan and the IHCAP, federal support under the

[13] Under both the Commission's 25/75 Plan and the IHCAP, rural carriers would continue to receive support under the current support mechanisms. They would move to a forward-looking methodology no sooner than January 1, 2001.

Ad Hoc Plan would be distributed in a manner determined by the state commissions.

B. The Ad Hoc Plan Is Even Less Focused Than The 25/75 Plan And It Is Unable To Target The Supra High-Cost Areas In States Which Require Funding Assistance

The Ad Hoc Plan consists of at least five steps for determining and distributing high-cost support for both rural and non-rural LECs.[14] However, upon closer examination, the Ad Hoc Plan is architecturally deficient. The Ad Hoc Plan results in nothing more than a hopeful approximation of what predominantly rural and low-density states such as Montana, Wyoming, West Virginia or Vermont require in the way of federal support for the high-cost areas in their state.

The first problem with the Ad Hoc Plan is that it bases funding on statewide averages of cost. In this respect it is similar to the current Universal Service Fund ("USF") Plan which was designed in the 1980s, and worked well in a monopoly environment. IHCAP, on the other hand, is specifically designed to target support to those areas and customers who need it most to retain affordable service. It is designed for the competitive market of the 2000s where it will not be possible for lower-cost customers to be overcharged to support higher-cost customers. Any time costs are averaged, implicit subsidies are created. Another problem is that by creating statewide cost averages, costs are averaged among the separate telephone companies which serve the state. This could threaten the "competitive neutrality" provisions of the 1996 Act and prior Commission decisions in that the most likely

[14] Notice at 5.

competitors for LECs in rural areas would appear to be other incumbent LECs ("ILEC").

The South Dakota Public Utilities Commission ("SDPUC") has been critical of the Ad Hoc Plan and statewide averaging of costs: "Providing support on the basis of embedded costs [which is a prominent feature of the Ad Hoc Plan] means [competitive local exchange carriers] CLECs would receive or not receive funds based on the incumbents costs. This is not competitively neutral."[15] The SDPUC also criticized the Ad Hoc Plan because the Plan's use of embedded costs would require the continued collection of data about the ILECs' costs. Imposing this requirements on ILECs but not on CLECs would be "anticompetitive" according to the SDPUC.[16] Moreover, the Ad Hoc Plan would require the continued use of Part 32 Accounting and Separations which will become obsolete tools in the competitive market.[17]

In the Universal Service Order, the Commission concluded that existing mechanisms for providing federal universal service support to rural and non-rural LECs should be converted to support mechanisms based upon forward-looking economic costs, beginning January 1, 1999 for non-rural LECs and not sooner than

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[15] Ex Parte Meeting -- Proxy Costs Models -- Alternative Support Proposal, submitted by the South Dakota Public Utilities Commission, CC Docket No. 96-45, Feb. 24, 1998 at 3 ("SDPUC Ex Parte").

[16] Id. at 2.

[17] Id. at 3.

January 1, 2001 for rural LECs.[18] The Commission concluded at the outset that forward-looking costs should be used to calculate the cost of providing universal service for high-cost areas, because it best reflects the cost of providing service in a competitive market for local exchange telephone service.[19]

The Ad Hoc Plan rejects the Commission's conclusion that the support mechanism should be based on forward-looking costs in favor of a decided preference for using embedded costs:

> Embedded cost has been included in the plan for two reasons. First, embedded cost is an appropriate limit on forward-looking because it has not yet been demonstrated that forward-looking models are accurate in all cases. Errors can arise from a variety of sources.[20]
>
> Where costs are increasing, or where existing plant is largely depreciated, the embedded network (assuming adequate service) provides the economically efficient method of providing local exchange service. This can be true in areas where increasing labor costs, raw materials cost, or real estate values have been increasing. Where embedded plant is providing adequate service and has a lower cost than new plant, the use of embedded costs is preferable.[21]

Proponents of the Ad Hoc Plan are skeptical about any cost model which may be used to determine forward-looking costs. They say that "these models should be used cautiously to ensure that any residual errors do not create undesirable side

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[18] Universal Service Order, 12 FCC Rcd. at 8792-93 ¶ 26. In a speech delivered on Apr. 27, 1998, Commission Chairman William Kennard indicated that the 2001 deadline for rural LECs was somewhat arbitrary and likely would be extended. Remarks by William Kennard, Chairman, Federal Communications Commission to USTA's Inside Washington Telecom, Apr. 27, 1998 at 2.

[19] Universal Service Order, 12 FCC Rcd. at 8792-93 ¶ 26.

[20] Ad Hoc Plan at 19.

[21] Id. at 15.

effects."[22] "[E]ven if the proxy models were perfect, there are economic reasons to consider embedded costs. Even if the proxy models were perfectly accurate and embedded costs were reported with complete accuracy, in some areas of the country it may be that forward-looking costs are higher than embedded costs."[23]

The SDPUC does not support the Ad Hoc Plan.[24] It has been particularly critical of the Plan's use of embedded costs: "Using embedded [costs] penalizes states with older plant and high depreciation rates."[25]

Although the Ad Hoc Plan opts in favor of using embedded costs, it gives lip service to the two principal cost models under consideration by the Commission: the Benchmark Cost Proxy Model ("BCPM") and the HAI Model (formerly known as the Hatfield Model). The BCPM proponents have worked diligently with the Commission staff to refine the design of the BCPM to identify and target customers in high-cost areas with precision. The Ad Hoc Plan would allow cost models to be used in a given state, but only if the cost model produces a lower cost result than actual embedded costs. Moreover, the Ad Hoc proponents blunt the ability of a cost model to target high-cost subscribers in each state by suggesting that the outputs of both cost models should be averaged in what the proponents call a Blended Cost Model.[26] The Ad Hoc proponents further say that costs and the resulting amount of

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[22] Id.

[23] Id. at 19.

[24] See SDPUC Ex Parte.

[25] Id. at 1.

[26] Ad Hoc Plan at 15.

federal support available to LECs serving high-cost areas in a state should be determined using statewide "average" costs.[27]

In the end, the Ad Hoc Plan fails to target those supra high-cost areas in states such as Wyoming, Montana, Mississippi or Vermont which need the most support to preserve universal service.

Even though the Commission said in the Universal Service Order that the existing support mechanism for rural carriers will not be changed until at least January 1, 2001, the Ad Hoc Plan would treat rural LECs and non-rural LECs alike for purposes of high-cost support beginning January 1, 1999. The Ad Hoc proponents contend that by combining rural and non-rural LECs now, the Commission and the states "can avoid anticipated rulemakings, now planned for 2001 or after, relating to support for rural carriers."[28] Even though the 1996 Act recognizes differences between LECs based upon size for important policy reasons,[29] the Ad Hoc Plan totally ignores differences for high-cost support based upon a LEC's size and requires both rural LECs and non-rural LECs to be combined in a single system of statewide averaging. There is no evidence on the record that such an approach would be appropriate.

One very real complication and problem with the Ad Hoc Plan is its many layers of "hold-harmless" provisions. For example, ILECs are held harmless for the receipt of existing support payments from the existing federal USF. This could pose

[27] Id. at 14.

[28] Id. at 29.

[29] E.g., the rural telephone company exemption and exceptions in 47 U.S.C. § 251(f).

a problem in a state where "rural" ILECs draw from the USF, but the "non-rural" ILECs do not. In this case, if the hold-harmless constraint is applied, no explicit high-cost funding would be available to the non-rural ILEC, even though it may serve many high-cost rural customers who currently benefit from non-sustainable implicit supports.

The Ad Hoc Plan is a plan of approximation and averages. It inappropriately combines differently-sized carriers. It averages the output of the cost models. And, in the end, by relying upon statewide averaging, the Ad Hoc Plan fails to target support to those supra high-cost areas in a state which require assistance from the federal fund.

V. THE TELECOMMUNICATIONS INDUSTRY ANALYSIS PROJECT'S ("TIAP") PROPOSED MODIFICATIONS ARE STRUCTURALLY INADEQUATE

The TIAP does not recommend a specific proposal, but rather provides data to analyze several alternative proposals which have been made by other parties. U S WEST appreciates the work that TIAP has done to help bring a better understanding to the universal service issues.[30] We here comment on several of the alternatives which are documented in the TIAP paper:

A. 40/60 Proposal

This alternative proposes to increase the share of the costs of providing universal service to be covered by the federal fund from 25% under the Commission's 25/75 Plan to 40%. Under the 40/60 alternative, states would be

[30] U S WEST is a member of the TIAP team, and provides funding to TIAP.

responsible for funding the remaining 60% of the costs, rather than 75% under the Commission's current 25/75 Plan.[31]

In rural, low-density states such as Wyoming, the Dakotas or Mississippi, the 40/60 proposal fails to target or provide support for the supra high-cost areas where the support is required. Whether under the 25/75 Plan or the 40/60 Plan, costs are driven principally by density and distance. Without targeted funding, providing support for universal service in high-cost areas in any state requires that revenues earned by LECs in densely-populated urban areas be used to subsidize service in supra high-cost areas of the state.

Increasing the federal share of support from 25% to 40% across the board for all states may provide the states of Wyoming, the Dakotas or Mississippi with some additional federal funding. However, it does not alter the demographic reality that these states do not have large numbers of urban telephone subscribers who can help to provide support for the low-density high-cost subscribers in the rest of the state. Because of this, the burden on local rates for all subscribers in these states is not insubstantial, whether the state's share of supporting universal service is 75% under the 25/75 Plan or 60% under the 40/60 proposal. The population density and revenue base do not exist in states like these.

B. Density Zone Proposal

Another TIAP proposal is that the federal fund would provide 100% of the required support for universal service, i.e., 100% of the difference between forward-

[31] Telecommunications Industries Analysis Project, Payers and Receivers: Various Proposals for the High Cost Fund, filed Mar. 5, 1998 at 33 ("TIAP's Proposals").

looking cost and the revenue benchmark. However, this support would only be provided in one or two of the lowest-density zones served by non-rural LECs.[32]

No clear principles have been developed to determine how density would be measured or defined. Therefore, it is unclear how the "two" lowest-density zones would be identified for purposes of implementing TIAP's density option.

VI. THE SDPUC CORRECTLY IDENTIFIES THE NEED FOR SUPPORT FOR SUPRA HIGH-COST AREAS; HOWEVER, IT IS UNLIKELY THAT CONSENSUS CAN BE REACHED REGARDING THE COMPLEX CHOICE OF VARIABLES TO IMPLEMENT HIGH-COST SUPPORT BY JANUARY 1, 1999

Like the Colorado PUC Staff, the SDPUC agrees that supra high-cost areas in Midwestern and Western states create the challenge for federal and state mechanisms which will assure adequate support. The SDPUC offers two proposals: A Variable Benchmark Option which would provide 100% federal funding above a benchmark and a Variable Support Option where the percentage of federal funding above a benchmark would vary. Both proposals would replace the 25/75 Plan and would focus only on supra high-cost areas.[33]

Under the Variable Benchmark Option, the benchmark in each state would vary based upon (1) the state's forward-looking economic cost and (2) the state's ability to fund its share of universal service.[34] The SDPUC says that a low benchmark would be established for states that have a relatively low ability to fund

[32] Id. at 24.

[33] Additional Proposals, Comments of the South Dakota Public Utilities Commission, filed Apr. 24, 1998 ("SDPUC Proposal").

[34] Id. at 3.

their share of universal service and that a higher benchmark would be established for those which have a greater ability to fund universal service.[35]

Under the Variable Support Option, a single nation-wide benchmark would be established.[36] However, the amount of federal support for each state would vary depending on the state's ability to fund its share of universal service.

With both of its proposals, the SDPUC struggles to explain how a state's "ability" to fund universal service would be determined. It suggests that ratios comparing intrastate revenues to total revenues or intrastate traffic volumes to total traffic volumes could be developed. It also suggests that a ratio of lines in urban areas and in rural areas, that "a measure of local competition in the state,"[37] or combinations of these or other measures could be developed.

The number of variables implicit in both proposals would make it difficult to predict the size of the federal fund or the amounts of contributions and assessments needed to establish such a fund. Both options would appear to be capable of targeting federal support to the supra high-cost areas in a state. However, while both options are only conceptual at this time and both may warrant further study and analysis, U S WEST is concerned that the complexity of defining the variables and reaching consensus among the states, and between the states and the Commission, could threaten implementation of the federal high-cost fund by January 1, 1999.

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[35] Id.

[36] Id. at 4.

[37] Id. at 5.

The federal fund must be capable of targeting federal support to the supra high-cost areas. But it must also be implemented not later than January 1, 1999, because implicit subsidies in the interstate jurisdiction upon which carriers have relied to support universal service are going away as local competition takes hold.

U S WEST commends the SDPUC for agreeing that the 25/75 Plan would provide insufficient federal support for supra high-cost areas in a state and would force the state commissions to impose unreasonable surcharge levels on intrastate services in an attempt to fund their share of the support obligation. However, U S WEST believes that the two options proposed by the SDPUC may be too conceptual with too many undefined variables. U S WEST has reservations that either proposal could be implemented by the target date of January 1, 1999.

VII. THE COLORADO PUBLIC UTILITIES COMMISSION ("COLORADO PUC") STAFF'S PROPOSAL CORRECTLY IDENTIFIES THE NEED FOR SUPPORT FOR SUPRA HIGH-COST AREAS; HOWEVER, THE PLAN'S ABILITY TO TARGET SUPPORT TO THESE AREAS IS QUESTIONABLE

The Colorado PUC Staff advocates a plan called the Variable Share of Federal Support. Like the Commission's 25/75 Plan, the Variable Share Plan would use a single benchmark for all states. Unlike the 25/75 Plan, the percentage share of federal support would vary depending upon: (1) the magnitude of support required per line; and (2) the state's ability to support its share of universal service.[38]

The ability of the Variable Share Plan to target support to the supra high-cost areas in a state begins to be questionable when the Colorado PUC Staff says:

[38] Colorado PUC Staff Comments, filed Apr. 24, 1998 at 2.